

Published in:

Geoffrey Brennan and Giuseppe Eusepi (eds.) (2009). *The Economics of Ethics and the Ethics of Economics: Values, Markets and the State*. Cheltenham: Elgar: 131-144.

The deregulation of the political process: Towards an international market for good politics

Reiner Eichenberger and Michael Funk ¹

Abstract

Human welfare and individual freedom depend on politics. However, the politicians' incentives to care for the preferences of the citizens are weakened by three kinds of regulations of the political process. Firstly, in most countries only nationals and residents are allowed to run for political offices. Secondly, in the same way parties and firms are excluded. Thirdly, the compensation of politicians is fixed by law, and often much below the salary for a comparable job in the private sector. This paper proposes to abolish these regulations and to allow for an open market for politicians. We suggest that the effect of such deregulations would be outstanding: Policy suppliers become active in several countries and, thus, can establish an international reputation i.e. for sticking to the election promises. Moreover, increasing explicit prices for political services will crowd out the implicit ones, such as bureaucratic rents and resources from special interests. The deregulation program will strengthen the influence of weakly organized groups and the governments' incentives to pursue general welfare and to protect individual freedom.

1. Introduction

Elections are deemed to mediate the provision of public goods along the citizens' preferences. However, it is obvious that politicians often renege on their campaign promises and tend to be captured by powerful special interests; furthermore, they are tempted to create political business cycles. In order to increase the government's incentives to cater for the citizens' preferences, Public Choice scholars typically propose to adjust political institutions. Many authors focus on federalism and hence, on strengthening the citizens' exit option. Other scholars concentrate on increasing the impact of the citizens' voice in the democratic process, e.g., by institutionalizing direct democracy. But while high migration cost prevent federalism from achieving full efficiency (e.g. Epple and Zelenitz 1981), direct democracy cannot eradicate the asymmetric influence of special interests, although there are strong improvements over representative democracy (Frey 1994, Eichenberger 1999a), especially when direct democracy is combined with an extended role of elected auditors (Eichenberger and Schelker 2007).

In this paper, therefore, a new proposal for reform of the political process is presented, which targets both, the executive as well as the legislative branches. The concept aims directly at the political process, which is regulated by three kinds of restrictions.

- Protectionist rules: Almost everywhere, only nationals are allowed to run for political offices. Moreover, the candidates often have to live in their constituency.
- Production process regulations: Usually only individuals can run for office. Parties and firms are not allowed to do so, but have to nominate individual candidates.

Moreover, parties must be non-profit organizations, and their internal structure is heavily regulated.

- Price regulations: all explicit prices of political services, i.e. the salaries of politicians and state subsidies for political parties are fixed by law.

In this paper it is argued that such regulations hamper political competition, weaken the politicians' incentives and ultimately enable special interests to seize their rents.

Consequently, it is proposed to abolish them. From such a deregulation of politics the citizens benefit in a similar way as consumer benefit from the deregulation of the consumer-good markets. It strengthens the influence of the weakly organized social groups, and it enhances efficiency in politics. This proposal brings back the market into politics. We acknowledge that public goods often cannot be provided by markets but only by governments. But we argue that government politicians should be controlled by the incentives of a competitive market.

The deregulation of politics, as proposed in this paper, differs fundamentally from other politico-economic reform proposals.² It proposes new rules for the "game of politics" which strengthen the policy suppliers' incentives to cater for the citizens' preferences. However, it does not give any recommendation on political contents. Thus, the suggestion is not more market and less government. Indeed the deregulation of politics goes a decisive step ahead of federalism and direct democracy: By opening political constituencies for external policy suppliers, it adds the mobility of politicians to the mobility of citizens and firms. Moreover, the strict emphasis on the supply side complements the demand focus of direct democracy.

The remainder is organized as follows: The next section explores why politics so often deviates from the citizens' preferences. It emphasizes the role of incomplete information as well as incomplete contracts. Section 3 analyzes the impact of the above-mentioned

regulations on politics and outlines the consequences of political deregulation. Section 4 considers arguments which are potentially raised against the concept here proposed. The fifth section concludes.

2. Politics far from citizens' preferences

Four aspects shape the design of today's politics: (i) Politicians cater for their own interests which often diverge from the citizens' interest; (ii) social groups differ with respect to their organizational potential; (iii) campaign promises are not binding; and (iv) the citizens' information on the platforms and achievements of parties and politicians, as well as the politicians' information on the preferences of the citizens, is far from perfect. These four defects of today's politics result in two main effects.

2.1. Politicians and parties deviate systematically from citizens' preferences

Today's democratic elections do not effectively prevent politicians from deviating from the citizens' preferences. If citizens are dissatisfied with the selfish policy of the government, they will not automatically vote for the opposition party. They know that the politicians of the opposition parties would face the same constraints as today's government as soon as they were elected into government. Thus, citizens do not necessarily expect today's opposition to govern differently than the present government (e.g. Funk and Eichenberger 2007). Therefore, governments have some discretionary power to pursue selfish policies which result in larger budgets, less efficient government services, higher deficits, higher debts and more regulations than the citizens prefer.

Politicians furthermore prefer short-time policies because they face in each election a high probability of dropping out without perspective of pursuing an equivalent job. Therefore, the institutional design forces upon politicians a low value of continuation, which mitigates incentives to build up long-time reputational capital (Funk 2008). Yet, politicians and parties do not have any interests to improve political accountability. Rather they try to diminish political competition by harmonizing and centralizing policies, by erecting entry barriers for new parties as well as by designing laws on party finance which favor the established parties.

2.2. The influence of social groups is asymmetric

Well-organized social groups have a stronger influence on politics than weakly-organized groups for at least three reasons (e.g. Olson 1965, Lohmann 1998): Firstly, well-organized groups can supply politicians with more tangible resources, e.g., campaign contributions and lucrative positions in associations and firms. Secondly, they can supply politicians with more information on their members' preferences, and they can provide their members with better information on the performance of politicians and parties. A politician's incentives to cater for the demands of a specific individual are the higher the more he knows about the individual's preferences and the better the individual is informed on the politicians' behavior (e.g. Eichenberger and Serna 1996). A politician can target his policies more effectively at those groups about whom he is well-informed, and he can be confident that the well-informed groups attribute the respective benefits to him or her. Thus, politicians tend to use the resources they control to benefit the well-organized interest groups rather than weakly-organized groups such as consumers and tax payers.

Thirdly, well-organized groups are in a better position to make politicians complying with their campaign promises. They can better evaluate whether, why and to what extent politicians comply with their promises, and they have better means to sanction politicians who fail to perform. Therefore, promises to well-organized groups are more credible and more effective than promises to weakly-organized groups. Hence, politicians target serious promises mainly at well-organized groups, while they tend to appease weakly-organized groups with fair words aiming to induce expressive voting behavior (Brennan and Lomasky 1993).

No wonder today's politics mainly serves the interests of well-organized groups while the interests of weakly-organized groups such as consumers and tax-payers are systematically neglected. The resulting policies mainly serve to protect and create privileges and rents. Thus, they are short-sighted, status quo-oriented and distribution-focused, and do not center on allocative efficiency.

3. Regulation decreases and deregulation increases welfare

3.1. The supremacy of political competition

Political economics has convincingly established that political competition improves the citizens' welfare (e.g. Besley et.al. 2007). The asymmetries in favor of the established suppliers of politics, well-organized interest groups and short-sighted policies can be undermined by strengthening political competition. The concept of deregulating the

political process intensifies competition among the policy suppliers by allowing for a new type of competition between and within countries.

The deregulation of the political process has quite similar effects as the deregulation of markets in general. The decision and information problem of the voters is closely related to the one of consumers of goods and services. In the goods market, too, producers are selfish, competition is restricted, advertising is not fully credible and the consumers' and producers' information is far from perfect. But it is generally accepted that deregulation intensifies competition and forces producers to cater more closely for the preferences of the consumers. The globalization of markets via abolition of protectionist measures increases the consumers' menu of choice and weakens producer cartels. Enlarging markets strengthens the incentives of the producers to develop brand names with a credible international reputation, and it makes producers more independent from local pressure groups. In the following, these arguments are transferred to politics.

3.2. The limitation of political competition

In today's democracies, political competition is constrained by three kinds of regulations, which prevent democratic institutions to benefit from the healing forces of market competition.

Almost anywhere, only nationals are allowed to run for political offices. Moreover, politicians often have to live in their constituency during their term and even when campaigning. These provisions have a strong protectionist impact: The voters are only allowed to demand political services from national or local suppliers. Political competition is weakened and the leeway of national and local policy suppliers is

increased. They may even form outright policy cartels or collude in other ways, as foreign suppliers are not allowed to step in the market (on policy cartels see Grossmann and West 1994).

Moreover, in most countries, only individuals can run for office. While a party determines a list of candidates, it is always an individual who is elected. This procedure makes it even more difficult for the citizens (i.e. the principals) to control the politicians (the agents) because they have often less information on the individual candidates than on the parties as a whole. In fact, parties cannot fully tie their members of parliament and government to the party program. While they can exclude representatives who do not stick to the party program from the party, they cannot recall them from office.

However, collective reputation will only work if the respective group can punish and ultimately exclude a non-cooperative individual. If it cannot do so this has in fact the adverse effect of locking its members into low performance (Tirole 1996). Moreover, the exclusive focus on individual candidates reduces the flexibility of the supply side. That is, job-rotation and job-sharing among part time politicians as well as functional specialization becomes almost impossible.

Finally, the explicit compensations of politicians are determined by law. Candidates cannot supply better services for higher prices. Because explicit compensation is usually much below the salary a qualified candidates could earn in the private sector, explicit payments have to be matched by implicit compensations. Such compensations are traditionally provided by interest groups. This is one of the main channels, through which the special interests compete for influence. But the various groups' potentials to implicitly compensate politicians differ strongly. Thus, the constraints on explicit

transfers increase not only the implicit transfers, but also the strong influence of well-organized groups.

The abundant regulations weaken political competition and restrain new suppliers.

Today, politics nowhere is a contestable market. Foreign and non-local as well as profit-seeking suppliers are excluded, either directly by law or indirectly by the above-mentioned regulations. The capital owners of a firm can only realize profits when the revenue can easily be transferred within the firm. But only explicit revenue is easily transferable. Implicit payments are much more difficult to transfer. Usually, their value is specific to individuals, subject to asymmetric information and sometimes even at the limit of legality. Moreover, profit-seeking suppliers should be able to flexibly substitute underperforming employees, which will be impossible if individuals are elected but not firms.

Close regulations also impede market entry of new suppliers. Political entrepreneurs who detect new demands of the citizens quicker than others cannot easily found new parties and supply their program on a broad base, because they cannot effectively bind the prospective representatives to their platform. Rather, they have to select candidates who cater intrinsically for the same aims and who are believed by the voters to be credibly committed to these aims. This, however, is time-consuming, costly and often impossible.

3.3. The deregulation program

The various legal restraints weaken the positive forces of democratic competition, mitigate political accountability, and prevent successful policy supplier from

transferring their reputation to other constituencies. Therefore, it is here proposed to abolish these regulations.

Firstly, outside political supplier should be allowed to run for office. Today's rules of origin and residential requirements are abolished. Foreigners and non-residents are allowed to run for all offices. The effect of deregulation is quite similar to the economic effects of free trade. It increases the number of potential candidates and, thus, the competitive pressure, which also makes domestic producers more efficient. But there is also another more interesting incentive effect: In a closed political system the quality and performance of the opposition candidate defines the reelection benchmark and therefore the performance of the incumbent. In contrast, in an open market each actor has larger opportunities and thus more effective incentives. For instance, in today's politics the most able policy supplier have little incentives because they get reelected anyway. In an open market, however, the most able suppliers have the strongest incentives because they have a high probability of being elected in the most attractive constituencies (Funk 2008). Moreover, there is also a fruitful reputation effect: Honesty and success in one constituency raise credibility and, thus, the chances of being elected in other constituencies. In such an open market for politics it is profitable for a supplier to build up an international reputation for being a high quality and credible policy producer.

Secondly, parties and firms are allowed to directly run for political office, without nominating specific individuals (but, of course, individuals are still allowed to run). If such a firm is elected, it can delegate the task depending on the mandate; that is, it can also substitute new delegates for hitherto active ones and, thus, bring in specialists for the problems to be solved. This deregulation forces domestic and foreign policy

suppliers to stick more closely to their promises. Therefore, the credibility of campaign promises is increased. The market is opened for internationally active policy suppliers whose success depends on the professional competence of the organization as a whole rather than on the individual celebrity of their exponents. Some of the control problems of the political process are then shifted to the collective accountability mechanism of the firms, which have better means to control and discipline their members. Thus, internationally reputed private organizations can directly step into politics, such as well-known consulting firms or human rights watch and environmentalist organizations (see also Fisman and Werker 2007).

Thirdly, explicit revenues of politicians should be set by market mechanisms. The competition among jurisdictions for able politicians will most probably lead to increasing explicit compensations for politicians. However, differences in salaries between jurisdictions provide the politicians with forceful incentives to perform. Increasing explicit revenues crowd out implicit revenues and, thus, decrease the asymmetry among interest groups. The influence of the weakly-organized groups increases. Moreover, the market is opened for profit-seeking firms which are more dependent on explicit income than traditional policy suppliers. The explicit revenues of politicians can be increased to cover their full opportunity cost. Another, even more attractive, option is to design a market for determining the appropriate compensations. For instance, they could be determined in a process related to submissions for public orders. The suppliers could publicize their compensation demand before the election. If they are elected, they get the posted compensation. As another possibility, every citizen could be given a budget which he can allocate with a new type of a secondary vote to the politicians and parties he prefers. This strengthens the candidates' incentives to submit reasonable compensation demands.

3.4. Multiple advantages

The proposed reform substantially changes the political landscape. Successful politicians will start an international (or at least ‘interjurisdictional’) career, which allows them to transfer their reputation to more attractive constituencies. At the other end constituencies will actively look for suitable candidates, which they might try to poach by a higher salary. In addition to the traditional suppliers of politics, internationally active policy firms can run for office. If they are elected, they can delegate domestic and foreign professionals into parliaments and governments. Such firms have stronger incentives to stick to their campaign promises because they are more frequently engaged in election contests. Because their performance in one country influences their chances in another one, they depend much stronger on their reputation than traditional suppliers. Moreover, the voters can easier judge internationally active suppliers, because they can access a much larger sample of observations than for only domestically operating parties.

Internationally policy suppliers have much stronger incentives to stick to promises, which are against their own interest as political actors. This increases the chance of welfare-enhancing constitutional reforms which strengthen the influence of the citizens but are not in the interest of the political establishment, such as federalism or direct democracy (see Frey and Stutzer 2000, Kirchgässner, Feld and Savioz 1999, Eichenberger 1999). Today, political parties most often do not follow their promises to strengthen these institutions, because such reforms are against their interests as soon as they are part of the majority. In contrast, in an international market, parties have incentives to become political turn-around managers who have a reputation for

implementing institutional reforms that benefit the citizens but weaken the politicians' influence.

Increasing explicit revenues of politicians crowd out implicit revenues. This is a consequence of various mechanisms. Firstly, explicit compensations are paid by the state. The influence of the citizens increases, because they can decide on the allocation of compensations with their vote. Secondly, the suppliers have to build up an international reputation of not relying on implicit compensations. Thirdly, higher explicit compensations strengthen the incentives of new firms to enter the market, which increases the competitive pressure. Profit-seeking policy suppliers depend more heavily on explicit compensations than traditional parties. Fourthly, high explicit compensations have an effect similar to efficiency wages. When explicit compensations increase, losing one's job becomes more expensive. Thus, politicians try to stay in government, i.e. they are willing to adapt their policy to suit the citizens' preferences. It is well known that higher salaries of bureaucrats crowd out corruption (see, e.g., World Bank Development Report 1997).

Consequently, the differences between well and weakly organized groups become less important. Thus, policy aims increasingly at the citizens' preferences and caters less for specific interests. At the same time, market entry of new suppliers becomes more likely. Therefore, suppliers have to react quicker to new problems and unsatisfied demands. As the differences between the various suppliers are larger in an international market, producers find it increasingly difficult to form cartels. Finally, the deregulation of the political process leads to a new type of harmonization of politics. Citizens who wish closer international policy coordination can vote for suppliers who are active in various

countries. This new type of endogenous policy coordination strongly contrasts with traditional types of "world governments".

3.5. Opportunities abound

Deregulation enhances the efficiency of all political systems, be they presidential, parliamentary, proportional or majoritarian. The deregulation is even more beneficial when a country's present institutions perform badly. Thus, deregulation offers especially promising perspectives to countries which suffer from underdevelopment and internal conflicts.

In most developing countries, elections take place occasionally or even regularly (e.g. Barro 1997). During the election campaign, all the candidates usually condemn inefficiency, pervasive corruption and misuse of power. However, when a candidate is elected, the constraints change dramatically. The incentives of a president, a minister or a parliamentarian not to be corrupted are small. Frequently, the rules and the result of the forthcoming elections can be influenced (e.g., by gerrymandering, reforms of the electoral system or by outright fraud). Such strategies do not cost much votes, because the citizens know that such behavior is not specific to today's government and most opposition candidates would behave similarly. But as soon as a country deregulates its market for politics, the situation changes fundamentally. Then, reputed foreign policy suppliers (individuals and firms) can run for office which also increases the incentives of the domestic politicians to stick to their promises.

Political deregulation is also especially fruitful within federalist and strongly decentralized countries. Today, politicians at sub-national levels usually have to live in

the jurisdictions where they hold a political office. This restrains political competition. After the deregulation, politicians could run for office in various jurisdictions at the same time, and they could have several parallel mandates. This would not only strengthen political competition, but also solve a serious problem of highly decentralized political systems. While today's small-scale jurisdictions often have difficulties to find qualified (part time) politicians among their citizens, political deregulation (even if it applies to the sub-national level, only) allows the local jurisdictions to engage non-residential politicians. Such politicians could cumulate political positions in different jurisdictions. Thus, a career in local politics would become an attractive job opportunity even for highly qualified individuals. Moreover, politicians could economize on the economies of scale and scope inherent in doing related jobs for several jurisdictions.

4. Alleged problems

The idea of deregulating the political process meets stiff opposition by politicians. In the following, some of their standard arguments are discussed.

Assertion 1: "The citizens would not elect foreign and non-local politicians". This argument is typically brought forth without reference to empirical observations. However, there is evidence that citizens are willing to delegate power to foreign politicians as soon as this offers promising opportunities. After all, an increasing number of countries import large parts of their legislation, especially from multilateral organizations. An example is provided by the sheer number of countries whose population wishes to join the European Union, which inevitably involves delegation of

governmental power to foreign politicians. Also countries which unilaterally peg their currency to another currency, give away some of their decision power to foreign policy makers. Actually, it would be surprising if individuals never voted for foreign politicians; at least they consume foreign products, marry foreigners, work in foreign-owned firms or under foreign managers and have foreign nurses to take care of their children. Indeed, in the German State of Baden Württemberg where non-residents can run for the office of a mayor, almost 80 per cent of the elected mayors were initially outsiders. Finally, it has to be emphasized that the citizens' preferences for domestic politicians do not justify rules of origin for politicians. If the citizens strongly prefer domestic politicians, international policy suppliers are either not successful, or they have to adapt. They would mainly delegate local candidates, exactly as international consulting firms engage local consultants in order to satisfy their clients' respective demands.

Assertion 2: "Deregulation is expensive". It is argued that increasing explicit compensations of politicians increases the costs of the political process and makes the influence of money even more prevalent. However, explicit revenues partly substitute for implicit revenues. Moreover, there is no evidence that explicit compensations crowd out intrinsic motivations more strongly than implicit compensations (see Frey 1997). Finally, the cost of policy reforms should be evaluated against their beneficial effects. Obviously, the explicit compensations of the politicians are most often irrelevant when they are compared to the benefits of good politics. Finally, it has to be noted that the cost of politics can easily be reduced by decreasing the size of the parliaments. This measure would hardly have noticeable drawbacks. Thus, only few observers would argue that the US-Senate with its 100 members or the second chamber of Switzerland

(the "Ständerat") with 46 members do a worse job than the Italian parliament with 630 representatives or the German Bundestag with 672 members.

Assertion 3: "Deregulation hampers the poor". Sometimes, the concept of deregulating politics is criticized, claiming that it could be noxious for poor countries, because international policy suppliers are concentrating on rich countries. However, the opposite tends to happen. The open market for politics induces suppliers of politics to become active in those countries where they are needed most urgently. The deregulation of the explicit compensations allows them to appropriate part of the value added that they create. This stops the brain drain from, and even leads to an inflow of political human capital into, political hotspots. Therefore, there is no danger of a race to the bottom with respect to the quality of politicians. It pays for politicians to behave like turnaround managers, who enter firms with the largest unexploited opportunities. Still another incentive to supply political services in poor, troubled countries is the reputation which can be gained by doing a good job in such countries.

Assertion 4: "The proposal is utopian". Historically, in most countries foreigners were allowed to play a much more active role than they did in the 20th century. It was often by marriage and succession that foreign aristocrats became kings and princes. Sometimes, they even were elected as kings. For instance, in 1573 the Polish aristocracy elected the then 23 years old Henry III, the brother of king Charles IX of France, as king of Poland. But Henry returned to France already in 1574 after his brother's death and became king of France himself. Therefore, the Poles had to look for another king. In 1575, they elected Stephan IV Bathory, the prince of Transylvania, as their new king. He stayed in office until 1586 and is known to be one of the most successful Polish kings. Another example is provided by the French marshal Jean-Baptiste Bernadotte who was

elected king of Sweden in 1810. Up to the 19th century, foreigners on the throne were no exceptions, as is illustrated, e.g., by the first kings of Greece, Rumania and Bulgaria who were all born in Germany. But also high ranking ministers were imported. A well known example is Klemens Wenzel Metternich, the powerful Austrian minister, who was not only born in Germany but who also began his political career in Germany. Finally, our proposal is closely related to the podestà in the enormously prosperous Italian city states of the 12th and 13th century. In this governmental system non-local and foreign political entrepreneurs were elected as leader of city-states for a predetermined period of time, most commonly six month or one year. Because of the strict term limits - and quite unintended - a market for podestà was launched with several hundred participants and high gains for success, but also severe losses from failure (see Funk and Eichenberger 2006).

The role of foreigners as political decision makers is not confined to history. Today, international organizations have some features in common with our proposal. Other examples are provided by non-governmental organizations, which play an increasingly important role, not only at the international, but also at the national level even though they are often dominated by foreigners. In business firms and in academics, foreigners play an even more important role. It is commonplace that chief executives and professors are foreigners, or, at least, come from outside. Actually, nominations of external candidates are often seen as preferable to internal nominations.

The opposition against the deregulation of politics is related to the opposition against the deregulation of sports markets some years ago. In football and hockey for example, the player unions defended quotas and other restraints with the argument that the fans wanted to see domestic players. However, the recent experiences show the opposite.

With an increasing proportion of foreigners, the quality of the game as well as the enthusiasm of the fans raised dramatically. Actually, today even in national teams it is often a foreigner who is the most important man - the coach.

5. Summary and conclusions

Economic growth and development have been boosted by deregulation. In contrast to the economy, politics has been protected from the efficiency-enhancing forces of markets, competition and free trade. Thus, political reforms should unleash those forces by deregulating the political process. Deregulation means to mitigate those forces which hinder political competition: rules of origin for politicians, regulations of the production process and prescriptions on the compensations of politicians.

This program changes politics fundamentally by strengthening the incentives of both, local and non-local policy suppliers. Moreover, international policy entrepreneurs could run for office and delegate domestic and foreign specialists to the parliament and to government. Such international policy suppliers have much stronger incentives to stick to their promises than today's politicians and parties, because they depend on their international reputation. While the increasing explicit compensation for holding political offices crowds out implicit revenues, the asymmetries among well- and weakly-organized groups decrease. Thus, politics caters increasingly for the preferences of the citizens by promoting efficiency and individual freedom. Finally, the globalization of politics leads to a new form of policy coordination. As soon as some policy suppliers gain influence in many countries, politics gets coordinated almost automatically.

The concept here proposed differs fundamentally from most other proposal for policy reform. It is strictly process-oriented. It does not propose specific contents of politics, but it proposes new rules that strengthen political competition and, thus, the incentives of policy suppliers to cater for the preferences of the citizens.

The arguments brought forward against the concept of deregulating politics are neither convincing, nor is the idea utopian. However, it is evident that many members of the political establishment, who make a good living in today's protected political environment, are not enthusiastic about the idea.

Two questions remain to be clarified: Firstly, are additional institutional prerequisites necessary in order to prevent the abuse of power by international policy suppliers? It is noteworthy that international policy suppliers have strong incentives to propose effective institutional mechanisms that constrain themselves from abusing their powers because this enhances their credibility and election chances. Nevertheless, there is no damage when multilateral organizations develop a best practice standard for competition regulation, which specifies the market rules and bans the development of monopolies.

Secondly, the questions of how and where the deregulation of politics could be put into effect should be tackled. The deregulation is welfare increasing in every country. It is the more fruitful, the smaller a country and the worse the country's political situation. Additionally, incentives increase with the size of the market; that is every additional country deregulating its political system increases welfare in the other countries. However, deregulation is especially promising to countries with a federalist structure

and to countries which intend to strengthen federalism. Already the deregulation of politics within such countries promises important welfare gains. Finally, deregulation has good chances when it can follow the successful deregulation of the economic realm. In the European Union, for instance, the deregulation of politics with its "free movements of politicians" seems only to be the logical complement to the four well-known economic freedoms.

Notes

¹ Contact: Center for Public Finance, University of Fribourg, Switzerland, Bd. de Péroilles 90, CH-1700 Fribourg. Phone: +41 26 300 82 62/65, Fax: +41 26 300 96 78, E-mail: Reiner.Eichenberger@unifr.ch.

² The idea has first been developed in Eichenberger (1999b).

References

- Barro, Robert J. (1997), *Determinants of Economic Growth: A Cross-Country Empirical Study*. Cambridge: MIT Press.
- Besley, Timothy, Torsten Persson and Daniel Sturm (2007), *Political Competition and Economic Performance: Theory and Evidence from the United States*, mimeo.
- Brennan, Geoffrey. and Loren E. Lomasky (1993), *Democracy and Decision: The Pure Theory of Electoral Preference*. Cambridge: Cambridge University Press.
- Eichenberger, Reiner (1999a), 'Mit direkter Demokratie zu besserer Wirtschafts- und Finanzpolitik: Theorie und Empirie', in: Hans H. von Arnim (ed), *Adequate Institutionen: Voraussetzung für "gute" und bürgernahe Politik?* Berlin: Duncker & Humblot, 259-288.
- Eichenberger, Reiner (1999b), 'Dereguliert, liberalisiert und globalisiert die Politik! Ein politisch-ökonomischer Reformvorschlag', *Studia Philosophica* **58**, 99-121.
- Eichenberger, Reiner and Mark Schelker (2007), 'Independent and Competing Agencies: An effective Way to Control Government', *Public Choice* **130** (1-2), 79-98
- Eichenberger, Reiner and Angel Serna (1996), 'Random Errors, Dirty Information, and Politics', *Public Choice*, **86** (1-2), 137-156.
- Epple, Dennis and Allan Zelenitz (1981). The implications of competition among jurisdictions: Does Tiebout need politics? *Journal of Political Economy*, **89** (6), 1197-1217.
- Fisman, Ray and Eric Werker (2007), 'Local Company Politics: A Proposal', *Capitalism and Society*, 2 (1), 1-7.
- Frey, Bruno S. (1994), 'Direct Democracy: Politico-Economic Lessons From Swiss Experience', *American Economic Review*, **84** (2), 338-342.
- Frey, Bruno S. (1997), *Markt und Motivation: Wie ökonomische Anreize die (Arbeits-)Moral verdrängen*, München: Vahlen.
- Frey, Bruno S. and Reiner Eichenberger (1996), 'To Harmonize Or To Compete - That's Not The Question', *Journal of Public Economics*, **60** (3), 356-349.
- Frey, Bruno S. and Alois Stutzer (2000), 'Maximizing Happiness?' *German Economic Review* **1** (2), 145-167.
- Funk, Michael (2008), 'Political Market Design', mimeo

- Funk, Michael and Reiner Eichenberger (2007), 'It's the Challenger, Stupid! Elections and the Theory of Rank-Order Tournaments', *CREMA Working Paper 2007-20*.
- Funk, Michael and Reiner Eichenberger (2006), 'Strangers in Politics. The Market for Good Politicians in Medieval Italy and its Lessons for Modern Democracy', mimeo.
- Grossmann, Philip J. and Edwin G. West (1994), 'Federalism and the Growth of Government Revisited', *Public Choice*, **79** (1-2), 19-32.
- Kirchgässner, Gebhard, Lars P. Feld and Marcel R. Savioz (1999), *Modern, erfolgreich, entwicklungs- und exportfähig: Die direkte Demokratie der Schweiz*, Basel: Helbing und Lichtenhahn.
- Lohmann, Susanne. (1998), 'The Information Rational for the Power of Special Interests', *American Political Science Review*, **92** (4), 809-827.
- Olson, Mancur (1965): *The Problem of Collective Action. Public Goods and the Theory of Groups*, Harvard University Press.
- Tirole, J. (1996), A Theory of Collective Reputation (with applications to the persistence of corruption and to firm quality), *Review of Economic Studies*, **63**, 1-22.
- Wiesendahl, Elmar (1999), *Entwicklung zu „Kartellparteien“?*, in: Hans H. von Arnim (ed.), *Adequate Institutionen: Voraussetzung für "gute" und bürgernahe Politik?* Berlin: Duncker & Humblot, 49-73.
- 'World Bank Development Report' (1997). Washington: The World Bank.